IN THE

# Supreme Court of the United States

OCTOBER TERM, 1971

No. ..... 71-1075

JACOB FERSHTMAN, HAROLD SIEGEL, ISABEL WEST, ZITA GARFIELD, LARRY SOMMA, HYMAN FREYDBERG, RENA KLEIN, JACOB KRIVILOFF, AGNES SHOEMAKER, as Executrix of the Estate of ROBERT SHOEMAKER, individually and as Limited Partners of PENN ASSOCIATES, a New York Limited partnership,

*Petitioners,*

*-against-*

HERMAN J. SCHECTMAN, SIDNEY P. SCHECTMAN, JOHN D. BUSSEL, HENRY SPELLMAN, GEORGE ZUCKERMAN, individually, and as General Partners of PENN ASSOCIATES, PENN ASSOCIATES, 461-8TH AVENUE CORPORATION, ROSE W. GROSS, as Executrix of the Estate of SIMEON F. GROSS and ELLIOT S. GROSS, co-partners doing business under the firm and style of "Simeon F. Gross and Elliot S. Gross", ROSE W. GROSS as sole distributee of the Estate of SIMEON F. GROSS, ELLIOT S. GROSS and ARTHUR YOUNG & COMPANY,

*Respondents.*

## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT


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## TABLE OF CONTENTS


| | Page |
|---|---|
| Table of Authorities | ii |
| Opinions Below | 1 |
| Jurisdiction | 2 |
| Questions Presented | 2 |
| Statutes and Regulations Involved | 3 |
| Statement of the Case | 5 |
| A. Basis for Federal Jurisdiction | 5 |
| B. Parties and Cause of Action | 5 |
| C. The Facts | 6 |
| 1. The Formation of the Partnership | 6 |
| 2. The "forced sale" involved | 9 |
| Reasons for Granting Writ | |
| I. The Decision Below Is In Conflict With the Applicable Decisions of This Court and Raises Significant and Recurring Questions Concerning Actions Involving Federal Securities Law Jurisdiction. | 13 |
| II. The Decision Appealed From Conflicts With the Decision of the Court of Appeals for the Seventh | |

Circuit in Allico National Corp. v. Amalgamated Meat Cutters & Butchers W., 397 F2d 727 (1968). . . 18

III. Petitioner were "Forced Sellers". The Purchaser-seller Restriction Should Be Abolished. . . . 19

CONCLUSION . . . . . 20

APPENDIX A . . . . . 1a

APPENDIX B . . . . . 10a

APPENDIX C . . . . . 19a

APPENDIX D . . . . . 21a

APPENDIX E . . . . . 22a

## TABLE OF AUTHORITIES

*Page*

Cases

*Allico National Corp. v. Amalgamated Meat Cutters & Butchers W.*, 397 F2d 727 (7th Cir., 1968) . . . . . ii, 18

*Birnbaum v. Newport Steel Corp.*, 193 F2d 461 (2d Cir. 1952), cert. denied, 343 US 1956 (1952) . . . . . 3, 19

*Brod v. Perlow*, 375 F2d 393 (2d Cir. 1967) . . . . . 13, 17

*Coffee v. Permian Corporation*, 434 F2d 383, (5th Cir. 1970) 17, 19

*Hooper v. Mountain States Securities Corporation*, 282 F2d 195 (5th Cir. 1960) . . . . . 17

*Janigan v. Taylor,* 344 F2d 781, (1st Cir. 1965) ..... 20

*Meinhard v. Salmon,* 249 N.Y. 458 ..... 17

*SEC v. National Securities,* 393 U.S. 453 (1969) ..... 19

*Superintendent of Insurance of the State of New York v. Bankers L & Co. Co.* –US–, 30 L Ed 2d 128. .....13, 16

*Vine v. Beneficial Finance Co.,* 374 F2d 627 (2d Cir. 1967), cert denied 389 US 970 (1967); ..... 19

Statutes and Regulations:

Securities Act of 1933, Section 17 (a) 15 USC § 77q(a) ..3

Securities Act of 1933, Section 22, 15 USC § 77v

Securities Exchange Act of 1934;

Section 10(b), 15 USC § 78j(b) ..... 2,3,4,15,17

Section 27, 15 USC § 78aa ..... 5

28 USC § 1254(1) ..... 2

Rule 10b-5 of The Securities and Exchange Commission, 17 CFR Section 240.10b-5. .....2,3,4,15,17 19

III Loss, Securities Regulations Second Edition 1794 .... 20

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# PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this case on November 3, 1971. Petitioners' motion for rehearing was denied by order dated November 26, 1971.

## Opinions Below

The opinion of the Court of Appeals for the Second Circuit, 450 F2d 1357 (1971), is annexed as Appendix A and appears at pp. 1a-9a of the Appendix, *infra.* The opinion of the

District Court for the Southern District of New York is unreported and is set forth as Appendix B at p. 10a.

## Jurisdiction

The judgment of the Court of Appeals was entered November 3, 1971. A timely petition for rehearing was denied on November 26, 1971 and this petition for certiorari was filed within 90 days of that date. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

## Questions Presented

1. Did the Court below err in affirming the dismissal of the complaint for want of federal jurisdiction, where the record indicates a "forced sale" of the limited partners' security interests resulting from the self-serving declaration of termination of the partnership by the respondent general partners, in conflict with applicable decisions of the Supreme Court?

2. Are Rule 10b-5 and Section 10(b) violated, where general partners of a limited partnership, by the device or scheme of making a self serving unilateral declaration of termination of the partnership, fraudulently appropriate and convert the leasehold asset, by the transfer of the stock of the corporate respondent to themselves, without making any attempt to sell the leasehold asset of the partnership to fulfill their fiduciary obligation to turn the assets of the partnership into a profit for all?

3. Did the Court below err in affirming the dismissal of the complaint by narrowly interpreting the intent of Congress in passing the Federal Securities Laws by restricting federal jurisdiction instead of liberally construing said laws to prevent fraud and unjust enrichment?

4. Has the Court of Appeals, in holding the petitioners' complaint should be dismissed for want of federal jurisdiction in connection with the "forced sale" of limited partnership security interests, erroneously invoked the purchaser-seller restriction enunciated in *Birnbaum v. Newport Steel Corp.*, 193 F2d 461 (2d Cir., 1952) cert. denied, 343 U.S. 956 (1952), which restriction is an important principle of Federal Securities Law that should be abolished, but which has not been, and should be decided by the Supreme Court?

## Statutes and Regulations Involved

This is a derivative action brought by limited partners of Penn Associates to recover damages based on violations of section 17(a) of the Securities Act of 1933, 15 USC section 77q(a), and section 10(b) of the Securities Exchange Act of 1934, 15 USC section 78j(b), together with Rule 10b-5, 17 CFR section 240. 10b-5 of the Securities and Exchange Commission.

Section 17(a) of the Securities Act states:

> "It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly–
>
> (1) to employ any device, scheme, or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which

they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser."

Section 10(b) of the Exchange Act states:

"Section 10 It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Rule 10b-5 provides:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security."

## Statement of the Case

A. *Federal Jurisdiction.*

Federal jurisdiction in the District Court is based on United States Code, Title 15, sections 77v, 78aa.

Section 77v in part states:

"(a) The district courts of the United States, . . ., shall have jurisdiction of offenses and violations under this subchapter and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter."

Section 78aa in part states:

"The district courts of the United States, . . ., shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder."

B. *Parties and Cause of Action.*

Petitioners are nine out of forty-seven limited partners of

"Penn Associates", a New York Limited Partnership.* They instituted this derivative action under the Federal Securities Laws on behalf of Penn Associates to recover $2,000,000 compensatory damages from the defendants, representing the value of the leasehold assets of Penn Associates which the respondents fraudulently appropriated and converted. The individual general partners consumated the fraudulent scheme, aided and abetted by the other respondents.

*C. The Facts.*

**1. The Formation of the Partnership.**

In 1955, Albert Kaine was a New York accountant who had numerous clients owning drug stores. Respondents, Herman J. Schectman and his son, Sidney P. Schectman, were brokers specializing in the purchase and sale of drug stores. As such, Kaine had made their acquaintance. Some time prior to October 28, 1955, Messrs. Schectman approached Kaine stating the General Partner Respondents were forming a limited partnership (Whitney Realty Co.) to acquire a parcel of real estate. They asked Kaine if he and his clients would be interested in becoming limited partners, which they did.

Shortly thereafter in April, 1956, the Messrs. Schectman again advised Kaine that the general partners were syndicating Penn Associates for the purchase of a 16-1/2 year balance of a lease expiring November 30, 1971 and a subordinate mortgage on a parcel of real estate consisting of an office building located at 461 Eighth Avenue, New York City, and an adjoining parking lot. The rental from this acquisition, so they advised, was to be shared with the limited partners.

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*The general partners are the Respondents, Herman J. Schectman, Sidney P. Schectman, John D. Bussel, Henry Spellman and George Zuckerman.

The Schectmans asked Kaine if he and his clients would be interested in participating as limited partners in Penn as they had in Whitney. Kaine asked for the details and the Messrs. Schectman exhibited a sheet of paper showing operating figures for the preceding fiscal year. It was represented that $730,000 capital would be required with the Limited Partners contributing $400,000 and the General Partners contributing $330,000. Of the capital, $286,250 was required to cover the acquisition of the lease, $393,750 for the mortgage, and $50,000 was for working capital. The lease was represented by defendants as having good possibilities of appreciation in value as rents increased and, upon the sale thereof, all the partners would share capital gain in proportion to their cash capital contribution and would, as well, enjoy their share of increased rents until the lease was sold.

Kaine discussed the proposition with his clients and friends, the plaintiffs in the instant action and the *Kaine* action, (hereafter referred to) and notified Messrs. Schectman they were agreeable to purchase limited partnership interests. Twelve of the limited partners, contributing over $50,000, were brought in by Kaine.

Early in May, 1956 the limited partners were notified by the general partners that all partners, including defendants, would have to contribute their capital. No proposed written partnership agreement was presented to them nor was mention made that they would later be required to execute a written partnership agreement.

A few days after the limited partners had contributed their cash capital contribution, they were contacted late on Friday.

May 4, 1956, and told they would have to attend at the general partners' offices to sign partnership papers on the next day, Saturday, May 5, 1956, otherwise they might lose out on the deal or lose out on at least a month's rent. Those of the partners who responded they would not be able to attend on Saturday either agreed to attend on Monday, May 7, 1956, or the managing partners had the papers delivered to their homes or places of business over the weekend where they were signed.

Copies of the partnership agreement or certificates were not distributed to the limited partners before they were submitted to them for signature. The general partners admitted on deposition that no limited partner was represented by counsel or had an opportunity to consult with an attorney or show the agreement or certificate to such attorney. Signatures were obtained by circulating two (2) copies among the 47 limited partners on Saturday and Monday, May 5th and 7th, so that the certificate of limited partnership could be filed in the New York County Clerk's office on Monday, May 7, 1956, in order that the closing, which had been scheduled for that day, could take place.

Kaine was not able to come to the Schectman's office on Saturday, May 5, 1956 as requested and so the Schectmans dispatched the proposed partnership agreement and certificate of limited partnership to his home in Mount Vernon, New York. On a casual reading of the documents by Kaine contradictory language in paragraph 8 of each were confusing in the light of the technical legal step-by-step provisions contained in paragraphs 6, 8 and 14 of the partnership agreement, which paragraphs when read together seemed to provide that the partnership could only terminate upon the sale of the lease prior to its expiration.

The difference in the language of both paragraphs "8" and the language in paragraph 6 raised a question in Kaine's mind whether the documents could be construed that the general partners could arbitrarily elect to pay off the limited partners at any time as if they were creditors of the partnership rather than only upon a sale of the leasehold as previously represented. Accordingly, before signing, Kaine called the Schectmans who assured him that the intention was that the partnership could only be terminated upon a sale of the lease or the termination of the partnership's interest in the venture. These respondents told Kaine to sign the agreement and certificate and to instruct his associates to do likewise because it had to be filed on Monday, May 7, 1956, in order to give legal effect to the partnership, and that respondents would confirm their understanding in writing.

Accordingly, Sidney Schectman wrote a letter, dated May 14, 1956, in which he assured plaintiffs as follows:

> "* * * the general partners can only pay off the limited partners in the event that the leasehold of the office building is sold." (App. C, p. 19a)

**2. The "forced sale" involved.**

By letter, dated March 29, 1968, to which was attached respondents' Arthur Young & Company statements, dated March 31, 1968, the general partners notified the limited partners of their unilateral declaration of termination of the partnership.

On receipt of this letter and being cognizant the lease had three and one-half more years to go and that no mention was made of the sale of the lease and distribution of capital gain, Kaine consulted his attorney who thereafter caused a search to

be made of the applicable land records. This search disclosed, theretofore unbeknown to petitioners, a 20-year extension of the lease on the premises to December 31, 1988 in favor of the respondent 461-8th Avenue Corporation, as lessee. The extended lease was dated as of January 1, 1968, signed on behalf of the respondent 461-8th Avenue Corporation by the general partner Sidney P. Schectman, as an officer thereof. The address of the corporation, shown on said lease, was c/o H. Schectman & Sons, said respondents drug store brokerage firm at 1440 Broadway, New York.

Upon discovery of respondents' appropriation of the extended lease, Kaine and two of the limited partners instituted a derivative action on behalf of Penn Associates against the general partners and their alleged wholly-owned 461-8th Avenue Corporation, for a judgment declaring defendants constructive trustees on behalf of the partnership of the lease (hereafter referred to as the "Kaine" action*).

On deposition of the general partners in the "Kaine" action, the limited partners first became aware of certain other undisclosed facts, i.e.

(a) Although the March 29, 1968 notice to limited partners stated "the general partners have elected to return to the Limited Partners the balance of their capital contributions, and to *terminate the Limited Partnership*, effective March 31, 1968", on August 21, 1969, almost a year and one-half later, on the deposition of one of the defendants Penn Associates was still in existence;

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**The petitioners moved in the District Court for consolidation or joint trial of both actions for judicial economy which the District Court denied.**

(b) In order to obtain the extended lease as of January 1, 1968 to December 31, 1988 the general partners had to release to the owners of the fee part of the leased premises consisting of a parking lot which brought in $10,000 a year rental which the limited partners shared in computing the overage of rents;

(c) The extended lease had become more valuable, yet the defendants made no effort to turn it into a capital gain profit;

(d) The general partners contemplated terminating the partnership upon obtaining the extension to the lease.

(e) Title to the lease had been originally taken in the name of the respondent 461-8th Avenue Corporation, which was capitalized at $300. The reason advanced for taking title to the lease in the name of the corporate respondent was (i) to limit personal liability for rent and (ii) the lease from the owner of the fee permitted only one assignment which was being exercised on its purchase. By taking title to the lease in the name of the corporation, respondents contended it would permit the sale of the lease asset by a sale of the stock of the corporation and thereby permit the distribution of capital gain to all partners.

(f) The stock of the respondent corporation was issued to one Simeon F. Gross, who was the undisclosed general partners' attorney. Until his death in 1964 he or his son, respondent Elliot S. Gross, filed corporate income tax returns stating he was the sole stockholder and president, which was attested to under penalties of perjury by the respondent, Arthur Young & Company. On Simeon F. Gross's death in December, 1964, his estate disclaimed

ownership of the stock to avoid including it as an asset of his estate, whereupon, his son, the respondent, Elliot S. Gross, transferred the stock to the General Partners without any consideration, although on deposition the general partners testified the stock was held by his father for the benefit of the partnership.

(g) The general partners paid no consideration for the transfer to themselves of the stock of the respondent corporation and were aware that taking the extension of the lease in the corporate respondents name they would become the exclusive owner of the lease upon declaring the partnership terminated.

(h) The general partners had entered into an operating agreement with the corporate respondent whereby the profits of the venture were to be shared 95% to the partnership and 5% to the corporate respondent. Even this arrangement was not adhered to, for it was profitable for the general partners to siphon all the tax benefits of the amortization of the cost of lease acquisition and leasehold improvements into the corporate defendant for the exclusive benefit of the general partners, and, accordingly, sufficient income of the partnership was transferred to the corporation each year to cover the aforesaid tax benefit deductions.

## REASONS FOR GRANTING WRIT

### I.

**The decision below is in conflict with applicable decisions of this Court and raises significant and recurring questions concerning actions invoking Federal Securities Law jurisdiction.**

The decision of the Circuit Court is in direct conflict with the decision of this Court in *Superintendent of Insurance of the State of New York v. Bankers L. & C. Co.*, ---- U.S. ----, 30 L.Ed.2d 128. The Court below handed down its decision November 3, 1971, five days before this Court's decision in *Supt. of Insurance, supra,* (November 8, 1971). Petitioners timely moved for a rehearing based on *Supt. of Insurance, supra,* which the Circuit Court denied. The Second Circuit's opinion in this case (App. A. pp. 1a-9a) represents important statutory and policy considerations emanating from a bona fide effort to invoke federal jurisdiction under the Federal Securities Laws. Efforts to invoke federal jurisdiction under the intention of Congress in enacting the Securities Laws are numerous. In many, the fraud are not the garden type associated with the purchase and sale of securities but may be as unique as the ingenuity of clever but not too conscientious minds can fraudulently devise. *Broll v. Perlow,* 375 F.2d 393, 397 (CA 2, 1967).

The Court below dismissed the complaint for "want of federal jurisdiction". In arriving at this conclusion it assumed by going outside the record that the attorney who may have composed part of the letter from the respondents to Kaine dated May 14, 1956 (App. "C" p.19) "was manifestly wrong." No trial testimony with available cross examinations, depositions or affidavits was available to the Circuit Court in arriving at this conclusion.

Considering the circumstances under which the partnership agreement and certificate of partnership were signed as heretofore described, a side by side comparison of paragraphs 8* in each of the documents is helpful to understand the doubt in petitioners' minds when the documents were presented for signature in the light of the representation that the parties were going into this venture to convert ordinary income into capital gain by a sale of the leasehold after rents were increased.

Paragraph 8 of the Certificate of Limited Partnership seemed to permit the return of the capital contributions of the Limited Partners at any time in the sole discretion of the General Partners with no reference to pro rata capital gain distribution provided for in paragraph 14 of the Partnership Agreement.

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*Partnership Agreement*

"8. The contributions of the Limited Partners to the capital of the partnership may be returned to them in whole, or in part, at any time, in the sole discretion of the General Partners, provided that all repayments of capital shall be pro rata among all the Limited Partners, *subject to the provisions of paragraph 14.*

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*Certificate of Limited Partnership*

"8. The contributions of the Limited Partners to the capital of the partnership may be returned to them in whole, or in part, at any time, in the sole discretion of the General Partners, provided that all repayments of capital shall be pro-rata among all the Limited Partners, *and further provided that in the event of the sale of the leasehold on premises 461 Eighth Avenue, New York City, the balance of the contribution of each Limited Partner shall be repaid in full.*

Contrary to paragraph "8" of the Certificate of Limited Partnership, paragraphs "6", "8" and "14"* of the partnership agreement are mutually supporting and not exclusive of one another and when read in conjunction with respondents' letter to Kaine dated May 14, 1956 (App. C.p.19a), where respondents state "[w]e would rather have had more time," makes it crystal clear that "* * * the general partners can only pay off the limited partners in the event that the leasehold of the office building is sold", and clearly indicates that unless the partnership interest in the leased property expired, the partnership could only be terminated if the lease was sold.

The general partners' March 29, 1968 unilateral declaration of termination of the partnership was misleading in that it represented that the partnership was being terminated

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*"6. The partnership shall commence on the date of filing the Certificate of Limited Partnership in the Office of the County Clerk of New York County. The partnership shall terminate on the 30th day of November, 1971, unless sooner terminated by either:

(a) a sale of the leasehold on the office building; or

(b) repayment of the contributions of the Limited Partners in full, as is more particularly hereinafter set forth;*

(c) retirement, death or insanity of a General Partner.

"8. The contribution of the limited partners may be returned to them * * * *subject to the provisions of paragraph 14.*"

"14. In the event that the agreement dated the 4th day of May, 1956 between 461-8th Avenue Corporation and partnership is cancelled *by reason of the sale of the leasehold on the office building*, then the Limited Partners shall be entitled to receive the following sums:

(a) Return of balance of capital contributions; and

(b) Twelve (12%) percent interest on such balance to be computed from the commencement of the current fiscal year, or the date of the most recent profit distribution, whichever period is shorter; and

(c) Ratable portion of the *capital gain* realized *upon such sale* on the proportion that the original capital contribution of each bears to SEVEN HUNDRED THIRTY THOUSAND ($730,000.00) DOLLARS."

whereas it was not and no disclosure was made of the 20 year extension of the lease which respondents appropriated thereby.

Section 10(b) and Rule 10b-5 prohibit among other things, the use of manipulative or deceptive devices, schemes, or contrivances to defraud or engage in any act which operates as a fraud or deceit upon any person and the omission to disclose material facts "in connection with the purchase or sale of any security." Section 10(b) and Rule 10b-5 further required the March 29, 1968,* "notice of termination of the partnership" not be misleading and required it to disclose the fact that the respondents had obtained a 20 year extension by releasing the parking lot the rental from which petitioners shared and the fact that because respondents had transferred the stock in 461-8th Avenue Corporation in whose name they had taken the extension of the lease upon the death of their attorney, the legal effect was they became the sole owners of the lease.

The fraud practiced on the limited partners and the unjust enrichment of the general partners by the appropriation and conversion of the valued leasehold is summarily disposed of by the Court of Appeals by narrowly interpreting the intention of Congress in passing the Federal Securities Laws. The opening sentence of its opinion indicates the restrictive approach to federal jurisdiction under the Federal Securities Acts in this Circuit. To the contrary, five days after the Circuit Court rendered its opinion this Court rendered its opinion in *Superintendent of Insurance v. Bankers L & C Co.* ——— U.S. ——— 30 L.Ed.2d 128, stating:

> "The Congress made clear that 'disregard of trust relationships by those whom the law should regard as

*"Under the provisions of Section 6 and 8 of the Limited Partnership Agreement of Penn Associates dated May 4, 1956, the General Partners may at any time elect to terminate the Partnership. Pursuant to the provisions of *these* Sections, the General Partners have elected to return to the Limited Partners the balance of their capital contributions, and to terminate the Limited Partnership, effective March 31, 1968."

> fiduciaries, are all a single seamless web' along with manipulation, investor's ignorance, and the like. * * * Hence we do not read § 10(b) as narrowly as the Court of Appeals; it is not 'limited to preserving the integrity of the securities markets' (430 F2d, at 361), though that purpose is included. Section 10(b) must be read flexibly, not technically and restrictively. Since there was a 'sale' of a security and since fraud was used 'in connection with' it, there is redress under § 10(b), whatever might be available as a remedy under state law. * * * The controlling stockholder owes the corporation a fiduciary obligation – one 'designed for the protection of the entire community of interests in the corporation – creditors as well as stockholders.' Pepper v. Litton, 308 US 295, 306-307, 84 L Ed 281, 288, 289, 60 S Ct 238." *Id.*, at p. 133-134.

The General Partners who were in sole control of the partnership made no attempt to turn the leasehold asset of the partnership into a capital gain profit to be shared in by all partners. Instead, they utilized their position of control to appropriate and convert the lease. *Meinhard v. Salmon*, 249 N.Y. 458.

The Circuit Court overlooked what a different panel than the one sitting in the instant case said in *Brod v. Perlow*, 375 F.2d 393 (2 Cir. 1967):*

> The facts alleged in the complaint are not the garden type variety of fraud. Where jurisdiction is questioned these facts are to be accepted as true. And, the complaint should not have been dismissed, if, under any reasonable reading, it states a

*"[We do not] think it sound to dismiss a complaint merely because the alleged scheme does not involve the type of fraud that is 'usually associated with the sale or purchase of securities.' We believe that § 10(b) and Rule 10b-5 prohibit all fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception. Novel or atypical methods should not provide immunity from the securities laws." Id., at 397.

claim upon which relief can be granted. If reformation of the partnership agreement is needed, then this equitable remedy is permissible in a Federal Securities Law violation action (section 77v, Title 15, USC). *Coffee v. Permion Corporation*, 434 F2d 383 (5th Cir. 1970); *Hooper v. Mountain States Securities Corporation*, 282 F2d 195 (5th Cir. 1960).

The questions raised herein will clarify the scope of section 10(b) and Rule 10b-5 in many actions involving contractual and fiduciary relationships on which the Court of Appeals opinion has ruled erroneously and which should be resolved by this Court.

## II.

**The decision appealed from conflicts with the decision of the Court of Appeals for the Seventh Circuit in *Allico National Corp. v. Amalgamated Meat Cutters & Butcher W.*, 397 F2d 727 (1968).**

Petitioners are in an analogous position as the plaintiffs in *Allico National Corp. v. Amalgamated Meat Cutters & Butcher W.*, 397 F2d 727 (7th Cir. 1968). That case also involved a breach of contract. The defendants had agreed to sell certain shares of stock to plaintiffs. When after an elapse of time the defendants realized the stock had appreciated in value, they sold them to others, profiting by an additional $500,000. It was held, the defendants wrongful conduct was motivated by increased profit and in connection with its transaction with plaintiff. The Seventh Circuit held that defendants conduct was a device or scheme which operated as a fraud or deceit on plaintiffs whereby defendants were unjustly enriched and was actionable under Section 10b, Rule 10b-5 and Section 17(a). By affirming the dismissal of the complaint the Circuit Court below is squarely in conflict with the decision of the Seventh Circuit in *Allico National Corp. v. Amalgamated Meat Cutters & Butchers W., supra.* The conflict justifies the grant of certiorari to review the judgment below.

## III.

**Petitioners were "Forced Sellers". The purchaser-seller restriction should be abolished.**

The Court below in reaching its conclusion to affirm the dismissal of the complaint for want of federal jurisdiction narrowly determined the petitioners were not "forced sellers" since they "refused to sign papers evidencing the return of their capital".* In considering whether the declaration of termination of the partnership by the respondents constituted a "forced sale" as to the five petitioners who did not sign the papers, the question is: –what was the limited partners position after the general partners declaration that the partnership was terminated? It must be answered –they no longer had a security interest. This is in effect respondents' position. The repayment of the limited partners capital is only a formality. *SEC v. National Securities*, 393 U.S. 453 (1968); *Vine v. Beneficial Finance Co.*, 374 F2d 627 (2d Cir. 1967) cert. denied 389 U.S. 970 (1967); *Coffee v. Permian Corporation*, 434 F2d 383 (5th Cir. 1970).

In assuming the petitioners were not "forced sellers" the Circuit Court, in effect, utilized the purchaser-seller restriction enunciated in *Birnbaum v. Newport Steel Corp.*, 193 F2d 461 (2d Cir. 1952) cert. denied, 343 U.S. 1956 (1952) which should be abolished as a standard for actions under Rule 10b-5. In this case it results in unjust enrichment of the respondents in

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*This assumption is not a fact. Petitioners, Harold Siegel, Hyman Freydberg, Jacob Kriveloff, Agnes Shoemaker, etc., did sign the papers proferred by the General Partners and their capital was returned to them.

violation of all concepts of partnership and fiduciary obligation law. This is a case that certainly merits petitioners not be limited to the purchaser-seller doctrine whereby defendants escape accounting for profits and in the process are unjustly enriched. 111 Loss, Securities Regulations, Second edition 1794; *Janigan v. Taylor,* 344 F2d 781, (1st Cir. 1965).

This Court has never ruled on the purchaser-seller doctrine as determining Federal Securities Law jurisdiction to sue. Since this case clearly raises the issue, the Court should resolve it by granting the writ of certiorari.

## CONCLUSION

For the reasons set forth above, it is respectfully submitted that this petition for a writ of certiorari to review the judgment and opinion of the Second Circuit should be granted.

Respectfully submitted,

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February 1972.

# APPENDIX

## APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 107—September Term, 1971

(Argued October 6, 1971 Decided November 3, 1971.)

**Jacog FERSHTMAN et al.,**
**Plaintiffs-Appellants,**

**v.**

**Herman J. SCHECTMAN et al.,**
**Defendants-Appellees.**

Before FRIENDLY, Chief Judge, WATERMAN and SMITH, Circuit Judges.

Appeal from an order of the District Court for the Southern District of New York, Edward C. McLean, *Judge*, dismissing, on motion, a complaint seeking to invoke federal jurisdiction on the basis of alleged violations of the Securities Act of 1933, the Securities Exchange Act of 1934, and the SEC's Rule 10b-5.

Affirmed.

Friendly, J.

This case represents another attempt to invoke the antifraud provisions of federal securities legislation and the SEC's Rule 10b-5 to confer federal jurisdiction in a situation to which the statutes and rule do not apply.

Plaintiffs-appellants are nine of forty-seven limited partners in Penn Associates (Penn) suing both individually and

derivatively. Defendants are the general partners of Penn, Arthur Young & Company (Penn's accountants), and the 461–8th Avenue Corporation. Although the complaint is long and diffuse and contains many immaterial allegations, the nub of it is this:

The general partners formed Penn pursuant to a limited partnership agreement dated May 4, 1956, for the purchase of a lease, expiring November 30, 1971, and a partially amortized second mortgage on a parcel of real estate consisting of an office building at 461 Eighth Avenue, New York City, and an adjoining parking lot. The purchase was actually effected through the 461–8th Avenue Corporation, an entity wholly owned by the general partners. Penn loaned 461–8th Avenue its entire contributed capital, and took the second mortgage as security. Of the $730,000 stated capital of Penn, $400,000 was contributed by the limited partners, and $330,000 by the general partners. The general partners did not contribute their own funds, but rather took a bank loan for their stated commitment, posting the mortgage as security. This arrangement was clearly authorized by paragraph 15 of the partnership agreement.

The contributions of the limited partners were to be repaid at the rates of 4% per annum for the first five years of the partnership, 6% for the sixth through ninth years, and 8% for the tenth through fifteenth years. The annual net profits were to be divided so that the limited partners would receive 12% on the existing balance of their capital contributions plus their *pro rata* share of 25% of all rentals in excess of $815,000 in any one year.

*Appendix A*

Paragraph 6 of the partnership agreement provided:

> 6. The partnership shall commence on the date of filing the Certificate of Limited Partnership in the Office of the County Clerk of New York County. The partnership shall terminate on the 30th day of November, 1971, unless sooner terminated by either:
>
> (a) a sale of the leasehold on the office building; or
>
> (b) repayment of the contributions of the Limited Partners in full, as is more particularly hereinafter set forth; or
>
> (c) retirement, death or insanity of a General partner.

The cross-reference in subparagraph (b) was to paragraph 8, which read:

> 8. The contributions of the Limited Partners to the capital of the partnership may be returned to them in whole, or in part, at any time, in the sole discretion of the General Partners, provided that all repayments of capital shall be pro rata among all the Limited Partners, subject to the provisions of paragraph 14.

Paragraph 14 provided that if a collateral agreement between Penn and 461–8th Avenue Corporation should be cancelled by reason of the sale of the leasehold, the limited partners should be entitled to receive the balance of their capital contributions, interest at the rate of 12% per annum on these since the commencement of the current fiscal year or the most recent profits distribution, and a portion of the capital gain realized on

*Appendix A*

such sale in the proportion that the capital contribution of each limited partner bore to the total capital of $730,000. Finally, paragraph 13(b) gave the general partners the right to modify the agreement between Penn and 461–8th Avenue Corporation so as to extend the lease beyond November 30, 1971, and explicitly provided that "Such renewal or extension shall not extend the life of the limited partnership past the time set for termination in paragraph 6 herein."

The venture proved highly successful. As of March 31, 1968, a date whose significance will later appear, a limited partner making an initial capital contribution of $10,001.00 would have been repaid $6600 and would have received (or be entitled to receive) $13,426.75 in profits on the diminishing capital balances, an average return of some 18% per annum.

The rift in the lute developed when the general partners, having previously caused 461–8th Avenue Corporation to obtain a 20-year extension of the lease from January 1, 1968, sent the limited partners a notice, dated March 29, 1968, wherein the former "elected to return to the Limited Partners the balance of their capital contributions, and to terminate the Limited Partnership, effective March 31, 1968." Attached to the letter was a schedule, prepared by defendant Arthur Young & Company, showing the unreturned capital contributions and the undistributed profits to which each limited partner was entitled. The limited partners were requested to communicate with Penn's counsel to obtain the papers they would have to execute in order to obtain these balances. Most of the limited partners did this. Three of them, who are plaintiffs in another action in the District Court for the Southern District of New

*Appendix A*

York wherein federal jurisdiction is predicated solely on allegations of diverse citizenship, and the nine who are plaintiffs in this action, did not.

The complaint here claimed that "the cause of action hereinafter alleged arises under Section Nos. 12(2) and 17(a) of the Securities Act of 1933 as amended and Section 10(b) of the Securities Exchange Act of 1934 as amended, and Rule 10b-5 * * * of the Securities and Exchange Commission promulgated thereunder; and Section 352-c of the General Business Laws of the State of New York."[2]

The complaint, in addition to asking compensatory and punitive damages of $2,000,000 for the class of limited partners, a figure seemingly plucked from the atmosphere, appears to have as its main objective, a decree requiring continuation of the partnership. It alleges a wide variety of misrepresentations and non-disclosures in connection both with plaintiffs' purchase of the limited partnership interests[3] in 1956 and with their "forced sales" pursuant to the termination of the partnership in 1968. With respect to the former, it suffices to say that, with one exception hereafter discussed, none of the alleged misrepresentations and non-disclosures are shown either to have been material within this court's definition in *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 848-850 (2 Cir. 1968), *cert. denied*, 394 U.S. 976 (1969), or, to have caused any damage. With respect to the latter, if defendants were legally entitled to terminate the partnership on March 31, 1968, in their sole discretion, it would make no difference what they misrepresented or concealed, even if we assume in plaintiff's favor that this transaction constituted a sale. *See Levine v. Seilon, Inc.*, 439 F.2d 328, 332 (2 Cir. 1971); *Drachman v. Harvey*, — F.2d —, — (2 Cir. 1971), *reh'g in banc granted*, 2 Cir., September 21, 1971.

*Appendix A*

The one matter alleged in the complaint that may, or may not, give plaintiffs rights of some sort is this: In April, 1956, the limited partners were sent copies both of the partnership agreement, whose provisions with respect to termination have been quoted, and the certificate of Limited Partnership which was to be filed in the office of the county clerk. Paragraph 8 of the certificate read as follows:

> The contributions of the Limited Partners to the capital of the partnership may be returned to them in whole, or in part, at any time, in the sole discretion of the General Partners, provided that all repayments of capital shall be pro-rata among all the Limited Partners, and further provided that in the event of the sale of the leasehold on premises 461 Eighth Avenue, New York City, the balance of the contribution of each Limited-Partner shall be repaid in full.

This differed from the corresponding paragraphs of the partnership agreement in failing to make clear that in the event of the sale of the leasehold, the limited partners were also entitled to share *pro rata* in any capital gain. Kaine, who had taken the lead in recruiting some of the limited partners and is a plaintiff in the other federal action, called defendant Sidney Schectman, one of the leaders of the general partners, in regard to the discrepancy and, allegedly, a clarification of what events could terminate the partnership. This call produced a letter from Schectman stating that "We have a clarification on the provisions of paragraph 8 in the Certificate of Limited Partnership as outlined by Mr. Russell Wilde our attorney." The letter continued, "With specific reference to your inquiry, I quote." The quote was as follows:

> "A question has arisen with respect to the provisions of paragraph 8 in the Certificate of Limited Partnership

concerning the rights of the general partners to pay off the limited partners. The Certificate of Limited Partnership is filed in the County Clerk's Office and is to give notice to the public concerning the rights and obligations of the partnership. The rights, however, as set forth in that agreement are not controlling. The agreement that is controlling concerning the limited partnership is the partnership agreement itself. Paragraph 8 in that agreement provides that the general partners can only pay off the limited partners in the event that the leasehold of the office building is sold.

It is our understanding that the provisions of the limited partnership agreement will be the controlling provisions and that you, as a limited partner, may disregard the provisions of the Certificate of Limited Partnership. The reason no change was made in the Certificate of Limited Partnership prior to its filing was that time was of the essence and it had to be filed and no changes could be made within the time permitted."

The last sentence of the first paragraph not only went beyond the discrepancy between the certificate of limited partnership and the partnership agreement but was manifestly wrong. Perhaps what the attorney meant was that if the leasehold were sold, the general partners could not pay off the limited partners simply by returning their capital contributions and their stipulated share in profits to the date of sale. However, the language not only failed to convey this, but also misstated the conditions upon which the general partners could return the limited partners' contributions.

[2,3] Despite this we are unable to see how transmission of the attorney's view, even if we assume this came to plaintiffs'

attention, gives rise to a claim under the securities laws. It may well be that, upon discovering the difference between the letter and the partnership agreement, plaintiffs would have been entitled to rescission under § 12(2) of the 1933 Act, but this is the last thing they now desire. In an ordinary tort action for damages they would encounter the obstacle of contributory negligence, at least if the attorney's misstatement was merely negligent as distinguished from being fraudulent, see ALI, Restatement of Torts 2d § 552-A, contrast § 545-A (Tent. Draft No. 10, 1964), and, while we need not decide the point, we would suppose that if an action lies for damages as a result of negligent misrepresentation under the securities laws, the same would be true. See Note, Civil Liability under Section 10B and Rule 10B-5, 74 Yale L.J. 658, 688-89 (1965). Beyond that plaintiffs have suffered no damage from making their investments; rather they have reaped large profits. What they are really seeking is reformation of the partnership agreement to conform to the attorney's characterization of it. But we have held very recently that even a buyer defrauded in violation of the securities laws "is entitled to recover only the excess of what he paid over the value of what he got, not * * * the difference between the value of what he got and what it was represented he would be getting. * * *" *Levine v. Seilon, Inc., supra*, 439 F.2d at 334. Plaintiffs' efforts to bring themselves within the rule applied by some courts in favor of defrauded sellers confront the obstacle that if the partnership agreement governed, there was no fraud in connection with what they term a forced sale. On the other hand, if the letter on which they rely had the effect of reforming the terms under which the partnership could be terminated, their refusal to sign papers evidencing the return of their capital and their share of the profits was proper, and they are not "forced sellers" in any sense. All that they have is a claim for reformation based on state law.[4]

*Appendix A*

The district court dismissed the complaint for failure to state a claim on which relief could be granted. We think the dismissal should have been for want of federal jurisdiction. With that modification, the order is affirmed.

1. While plaintiffs frequently compare this to the conduct condemned in *Meinhard v. Salmon*, 249 N.Y. 458, 164 N.E. 545 (1928), the pellucid provision of paragraph 13 of the partnership agreement, cited above, makes the reference fall rather flat.

2. In view of our holding that the complaint did not state a claim under the federal securities laws, we need not consider the applicability of the New York statute. See *T.B. Harms Co. v. Eliscu*, 339 F.2d 823, 829 (2 Cir. 1964), *cert. denied*, 381 U.S. 915, 85 S.Ct. 1534, 14 L.Ed.2d 435 (1965).

3. Defendants concede these to have been "securities" within the meaning of the 1933 and 1934 Acts.

4. In light of the foregoing discussion, we need not consider the defenses of the statute of limitations and the special arguments presented by defendant Arthur Young & Company.

## Appendix B — OPINION

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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JACOB FERSHTMAN, HAROLD SIEGEL, ISABEL WEST, ZITA GARFIELD, LARRY SOMMA, HYMAN FREYDBERG, RENA KLEIN, JACOB KRIVILOFF, AGNES SHOEMAKER, as Executrix of the Estate of ROBERT SHOEMAKER, individually and as Limited Partners of PENN ASSOCIATES, a New York Limited Partnership,

Plaintiffs,

-against-

HERMAN J. SCHECTMAN, SIDNEY P. SCHECTMAN, JOHN D. BUSSEL, HENRY SPELLMAN, GEORGE ZUCKERMAN, individually and as General Partners of PENN ASSOCIATES, PENN ASSOCIATES, 461-8TH AVENUE CORPORATION, ROSE W. GROSS as Executrix of the Estate of SIMEON F. GROSS and ELLIOT S. GROSS, co-partners doing business under the firm and style of "Simeon F. Gross and Elliot S. Gross," ROSE W. GROSS as sole distributee of the Estate of SIMEON F. GROSS, ELLIOT S. GROSS and ARTHUR YOUNG & COMPANY,

Defendants.

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McLEAN, D.J.

This action involves a controversy between nine limited partners and five general partners of Penn Associates, a New York limited partnership, organized in May 1956 for the purpose, according to the partnership agreement, of "the operation, management and control of premises No. 461 Eighth

Avenue, New York City . . . and the ownership of the second mortgage on the fee of said premises." All the defendants move to dismiss the action for failure to state a claim, and the defendants other than Arthur Young & Company also move for a variety of other relief.

Prior to the institution of this action, another action was begun in this court entitled *Kaine, et al. v. Schectman, et al.*, 68 Civ. 2305, by three limited partners against the general partners and Penn Associates and 461 8th Avenue Corporation. Plaintiffs in that action are represented by the attorney who also represents the present plaintiffs. That action has been actively litigated and is still undetermined. Subject matter jurisdiction of that action is based on diversity of citizenship, the three plaintiffs being residents of Florida, whereas defendants are residents of New York. A motion by plaintiffs in that action to join Arthur Young & Company as a defendant was denied by Judge Pollack on September 9, 1969.

The nature of plaintiffs' claims and the relief asked in the two actions is very similar, with the exception that the Kaine action charges only a violation of state law, whereas the complaint in the present Fershtman action charges a violation of the federal securities laws. It is apparent that the present action is an attempt by limited partners who could not join the Kaine action because they are New York residents to maintain an action in this court similar to Kaine's against the same persons who are defendants in the Kaine action, and also against additional defendants whom Kaine was not permitted to sue in his action. Whether the present plaintiffs can accomplish this purpose depends upon whether their complaint states a federal claim under the securities laws, specifically Sections 12(2) and 17(a) of the Securities Act of 1933, and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

*Appendix B*

The "securities" are the interests in the limited partnership. No one disputes that these interests constitute securities within the meaning of the 1933 and 1934 Acts and for present purposes I will assume that they do. Plaintiffs are the buyers of these securities. The sellers are the general partners. The purchase took place in May 1956. Plaintiffs claim that the general partners induced plaintiffs to purchase their respective interests by affirmative misrepresentations and by concealing material facts. Most important of the affirmative misrepresentations is the statement allegedly made by the general partners that the partnership would continue until "(1) the lease on said premises or renewals thereof was sold or (2) terminated." Plaintiffs' principal grievance is that on March 29, 1968, almost twelve years after the purchase by plaintiffs of their limited partnership interests, the general partners notified plaintiffs that they had terminated the partnership, even though the lease had not been sold, but in fact had been renewed until December 31, 1988. There are other alleged misrepresentations in this exceedingly prolix complaint, but this seems to be the nub of the matter.

Alleging that this termination of the partnership in 1968 was "illegal, unlawful and in violation of the partnership laws of the State of New York," plaintiffs ask judgment (1) declaring 461 8th Avenue Corporation, Penn Associates and the general partners to be constructive trustees for Penn Associates and for plaintiffs of the leasehold, (2) requiring defendants "to account to Penn Associates as to the tax advantages" of certain transactions between Penn Associates and 461 8th Avenue Corporation, (3) "decreeing the interests of the plaintiffs and members of their class and the Managing Partners in accordance to their cash equity capital contributions to Penn Associates," and (4) "requiring defendants to account" for compensatory and punitive damages in the sum of $2,000,000.

Before considering whether this amounts to a claim under the federal securities laws against the general partners, I will first consider the case as to Arthur Young & Company, who was the accountant for the partnership. The complaint alleges that Arthur Young & Company "aided and abetted the Managing Partners in their misrepresentations, fraud, deceit and conspiracy hereinafter alleged." It alleges further that all the defendants "engaged in a continuing agreement, understanding, concert of action, plan, scheme and conspiracy" in the sale of the securities of Penn Associates to the plaintiffs. More specifically, the complaint alleges that Arthur Young & Company "caused false and improper statements and income tax returns to be prepared and distributed showing distribution of income to the limited partners." This allegation refers to events subsequent to the sale of the limited partnership interests to plaintiffs in 1956.

It is tolerably clear from the face of the complaint that Arthur Young & Company was not a seller of these limited partnership interests.* The conclusory allegation that it "aided and abetted" the sellers and "conspired" with the sellers is not enough to charge Arthur Young & Company with being a seller itself.

* Any possible uncertainty that conceivably could exist from the face of the complaint as to the nature of plaintiffs' real claim against Arthur Young & Company is dispelled by a lengthy affidavit submitted in opposition to this motion by plaintiffs' attorney. The affidavit is improper on a motion addressed to the face of the complaint, but reading it leaves no doubt that what plaintiffs are claiming is that Arthur Young & Company, in its capacity as accountant of the partnership, incorrectly handled the accounting.

*Appendix B*

*Barlas v. Bear, Stearns & Company*, 64-66 CCH Sec.L.Rep. paragraph 91674 (N.D. Ill. 1966)

As far as this defendant is concerned, the complaint seems to me to be a transparent attempt to state a federal claim against Arthur Young & Company when none in fact exists. Plaintiffs are at Liberty to sue Arthur Young & Company, if they so desire, in the state court, but they may not maintain this action against it here. For this reason, as well as for the additional reason discussed hereinafter with respect to the claim against the general partners, the complaint does not state a claim against Arthur Young & Company.

The other new defendants, not sued in the Kaine case, are the Gross defendants, *i.e.*, Rose W. Gross, as executrix of the estate of Simeon F. Gross, and Elliot S. Gross, co-partners doing business under the firm and style of "Simeon F. Gross and Elliot S. Gross," Rose W. Gross, as sole distributee of the estate of Simeon F. Gross, and Elliot S. Gross. Simeon Gross, now deceased, and Elliot Gross were the lawyers for the general partners. There is no direct allegation that they sold any securities to plaintiffs. As in the case of Arthur Young & Company, they are said to have "aided and abetted" the managing partners in their misrepresentations, and to have been parties to the "conspiracy." More specifically, the complaint charges the Grosses, in substance, with being dummy officers, directors and stockholders of 461 8th Avenue Corporation "for the sole purpose to conceal the true beneficial interest and identity of the Managing Partners of Penn Associates as the controlling stockholder, officers and director principals in 461 8th Avenue Corporation." According to the complaint, Simeon Gross died on December 31, 1963, some seven years after plaintiffs purchased their partnership interests, and it was "subsequent to the date of the death of said Simeon F. Gross"

that the managing partners became officers, directors and record owners of the stock of 461 8th Avenue Corporation.

Whatever kind of claim these allegations may be thought to allege against the Grosses, I do not think that the complaint can fairly be construed to allege that the Grosses were sellers of securities within the meaning of the federal securities laws. What has been said with respect to plaintiffs' claim against Arthur Young & Company applies to their claim against the Grosses as well.

This brings us to the claim against those defendants who have previously been sued in the Kaine action, *i.e.*, the general partners, Penn Associates and 461 8th Avenue Corporation. Penn Associates appears to have been named a defendant because the plaintiffs purport to sue on its behalf, although there would seem to be no basis for such a derivative action under the securities laws, since there is no allegation that Penn Associates purchased any partnership interest in itself. Just what plaintiffs' theory is as to 461 8th Avenue Corporation is wholly unclear. In any event, there is no allegation that this defendant sold securities to plaintiffs. As far as the general partners are concerned, however, there is no doubt that the complaint alleges that they were the sellers of the securities purchased by plaintiffs and that they sold them to plaintiffs on the strength of material misrepresentations and omissions.

The general partners base their motion to dismiss upon the contention that the complaint does not allege that the misrepresentations which induced plaintiffs to purchase the partnership interests in 1956 have caused plaintiffs any damage, or, at any rate, the type of damage recoverable for violations of the sections of the 1933 and 1934 Acts which plaintiffs claim were violated.

This contention is clearly correct as far as Section 12(2) of the 1933 Act is concerned. The complaint does not allege that plaintiffs have disposed of the securities, i.e., their partnership interests. Under these circumstances, Section 12(2) expressly limits plaintiffs to the right to "recover the consideration paid for such security with interest thereon . . . upon the tender of such security." In other words, plaintiffs' only remedy under this section is rescission.

*Pfeffer v. Cressaty*, 225 F. Supp. 756 (S.D.N.Y. 1963)

Plaintiffs do not allege any tender. It is manifest that they are not seeking rescission here. On the contrary, they seek to enforce their interest in the partnership.

After careful examination of the complaint, I have concluded that defendants are also correct as to the other sections involved, Section 17(a) of the 1933 Act, and Section 10(b) of the 1934 Act and Rule 10b-5. The damages recoverable for misrepresentations "in the offer or sale of any securities" (Section 17(a)) or "in connection with" the sale of any securities (Section 10(b) and Rule 10b-5) are tort damages representing plaintiffs' out-of-pocket loss. The rule has been stated, with the citation of many supporting authorities, in *Estate Counseling Service v. Merrill, Lynch, Pierce, Fenner & Smith, Incorporated*, 303 F.2d 927, 533 (10th Cir. 1962), as follows:

> "In the Federal courts the measure of damages recoverable by one who through fraud or misrepresentation has been induced to purchase bonds or corporate stock, is the difference between the contract price, or the price paid, and the real or actual value at the date of the sale, together with such outlays as are attributable to the defendant's conduct.

(or in other words, the difference between the amount parted with and the value of the thing received."

Plaintiffs are entitled to what they have lost, not to what they might have gained as the fruits of an unrealized speculation.

This complaint contains no allegations which fit this theory of recovery. Despite all its repetitious verbiage, it is reasonably plain from the complaint, read as a whole, that plaintiffs' grievance lies in the fact that the managing partners, many years after plaintiffs purchased their partnership interests, attempted to terminate the partnership. Essentially, plaintiffs' claim is one for breach of contract. The relief asked by plaintiffs, the declaring of the general partners to be "constructive trustees," the decreeing of the interests of the parties in the partnership "in accordance to their cash equity capital contributions," the requiring the general partners to account, etc., etc., is not in any sense the type of relief appropriate to an action for damages for violation of Sections 17(a) and 10(b).

These plaintiffs are asserting substantially the same claims as the Kaine plaintiffs asserted. These are state claims. They do not become federal claims merely by characterizing them as violations of the federal securities laws. There has to be some limit to the extent to which Section 17(a) and Section 10(b) can be stretched to encompass matters which they cannot reasonably be construed to include.

The motion of all defendants to dismiss the action for failure to state a claim is granted.

So ordered.

Dated: April 8, 1971

s/ Edward C. McLean
U.S.D.J.

# APPENDIX C

SIDNEY P. SCHECTMAN
1440 Broadway
New York 18, N.Y.
May 14, 1956

Mr. Albert Kaine
300 Hayward Avenue
Mt. Vernon, New York

Re: Penn Associates

Dear Al:

We have a clarification on the provisions of paragraph 8 in the Certificate of Limited Partnership as outlined by Mr. Russell Wilde our attorney.

With specific reference to your inquiry, I quote:

"A question has arisen with respect to the provisions of paragraph 8 in the Certificate of Limited Partnership concerning the rights of the general partners to pay off the limited partners. The Certificate of Limited Partnership is filed in the County Clerk's Office and is to give notice to the public concerning the rights and obligations of the partnership. The rights, however, as set forth in that agreement are not controlling. The agreement that is controlling concerning the limited partnership is the partnership agreement itself. Paragraph 8 in that agreement provides that the general partners can only pay off the limited partners in the event that the leasehold of the office building is sold.

It is our understanding that the provisions of the limited

partnership agreement will be the controlling provisions and that you, as a limited partner, may disregard the provisions of the Certificate of Limited Partnership. The reason no change was made in the Certificate of Limited Partnership prior to its filing was that time was of the essence and it had to be filed and no changes could be made within the time permitted."

I hope that this will satisfy your questions. We would rather have had more time, but there would have been no sense in losing a month's profits.

Best wishes.

Cordially yours,

s/ Sid

Sidney

SPS/sb

## APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

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Jacob FERSHTMAN et al.,
Plaintiffs-Appellants,

v.

Herman J. SCHECTMAN et al.,
Defendants-Appellees.

A petition for a rehearing having been filed herein by counsel for the appellants,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

Henry J. Friendly, Chief Judge

Sterry R. Waterman, USCJ

J. Joseph Smith, Circuit Judge

November 26, 1971.

## APPENDIX E

## UNITED STATES COURT OF APPEALS
## FOR THE
## SECOND CIRCUIT

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At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the third day of November one thousand nine hundred and seventy-one.

Present:

HON. HENRY J. FRIENDLY

*Chief Judge*

HON. STERRY R. WATERMAN

HON. J. JOSEPH SMITH

*Circuit Judges.*

Jacob FERSHTMAN et al.,
**Plaintiffs-Appellants,**

Herman J. SCHECTMAN et al.,
**Defendants-Appellees.**

*Appendix E*

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed as modified in accordance with the opinion of this court with costs to be taxed against the appellants.

A. DANIEL FUSARO
Clerk

[seal]

A true copy;
s/ A. Daniel Fusaro, Clerk